

**TESTIMONY REGARDING SENATE BILL No. 575**  
**AN ACT AMENDING ARTICLE 9 OF THE UNIFORM COMMERCIAL CODE TO**  
**PROHIBIT THE FILING OF RECORDS INTENDED TO HINDER, HARASS OR**  
**OTHERWISE WRONGFULLY INTERFERE WITH A PERSON**

**Presented By**

**Thomas J. Welsh, Esq.**

**March 11, 2002**

Good afternoon, my name is Thomas J. Welsh and I am a principal of the law firm of Brown & Welsh, P.C. located in Meriden, Connecticut. I am member of the Executive Board of the Association of Commercial Finance Attorneys and was a member of the Law Revision Commission Advisory Committee on Revised Article 9 that prepared the draft which became the text of P.A. 01-132, adopting Revised Article 9 of the Uniform Commercial Code effective October 1, 2001. I also testified on behalf of the Connecticut Bar Association and as the designated representative of the CBA Commercial Law and Bankruptcy Section in the adoption of Revised Article 9 in 2001. Although I am not testifying officially on behalf of the Connecticut Bar Association, since this matter is scheduled to be discussed at the Executive Committee of the Commercial Law and Bankruptcy Section at the end of this month, this testimony is based upon my knowledge and experience from my practice, from assisting in the adoption of Revised Article 9 and from my informal discussion with commercial lawyers and Executive Committee members prior to this hearing. In the event that these remarks are adopted as a position of the Connecticut Bar Association this fact will be communicated to you by Bar Association staff.

**I. INTRODUCTION**

A. **The Proposed Bill:** The goal of the proposed Bill is stated as being to amend Article 9 of the Uniform Commercial Code (referred to herein as "Article 9") to provide remedies for the wrongful filing of records intended to hinder, harass or otherwise wrongfully interfere with a person. The methods employed to achieve this goal are as follows:

1. To amend Section 9-518 of Article 9 (codified as Conn. Gen. Stat. §9-518) to:
  - Permit the Office of the Secretary of the State to reject a record presented for filing if the secretary determines that the record was not "created" pursuant to Article 9 or was intended for an improper purpose, such as to hinder, harass or otherwise wrongfully interfere with any person.

**BROWN & WELSH, P.C.**

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- Require a written certification, under oath, on a correction statement to the truth of the statements therein.
- Require the Office of the Secretary of the State to determine, without undue delay, whether any record alleged in a correction statement to have been wrongfully filed should have been rejected.
- Permit the Office of the Secretary of the State to cancel a record if it determines that it was wrongfully filed and should have been rejected.
- Provide an appeal process to the Superior Court from any such action by the Office of the Secretary of the State.

and

2. To provide a criminal penalty, in Section 4 of the Bill, for such wrongful filing, with knowledge that either: (a) the record is not related to a valid security agreement; or (b) with the intention to hinder, harass or otherwise wrongfully interfere with any person.

**B. Treatment of Wrongful Filings Under Current Article 9:** Revised Article 9 of the Uniform Commercial Code was adopted in Connecticut by the General Assembly in the 2001 session and signed by the Governor on June 14, 2001. It went into effect in Connecticut on October 1, 2001 and in virtually<sup>1</sup> all of the other 50 states and the District of Columbia on July 1, 2001. Revised Article 9 made significant revisions to secured transactions law and the concepts underlying the filing system. It is an extremely complex and tightly drafted statute, so any revision to Article 9 must be carefully considered to determine the effect of the change in numerous circumstances. In the brief time that Revised Article 9 has been in effect, there has been insufficient time to determine cases and collect statistics regarding the extent of wrongful filing, however in light of problems under old Article 9 relating to forged signatures and the deletion of any signatures on the new Article 9 forms, the Drafting Committee of Article 9 dealt with the potential of such filings in several ways.

1. **"Open Drawer" Filing System and Effect of False Filings:** Article 9 now provides, in §9-519, that all filings relating to a financing statement are to be maintained for a minimum period of one year after the lapse of the subject financing statement. This rule applies even if the filing office accepts a record purporting to delete or modify the name of a debtor or to terminate the effectiveness of a filed financing statement. The stated intention was to increase the amount of information available to those who search the public records and "contemplates that *searchers – not the filing office – will determine the significance and effectiveness of filed records*" (Emphasis added) *Comment 6, §9-519* As *Comment 2 to Section 9-509*, dealing with parties who are authorized to file records, notes, "[t]he question of authorization [for the filing of a record] is one *for the court, not the filing office.*" (Emphasis added) Section 9-510(a) provides, however,

<sup>1</sup> Alabama, Florida, and Mississippi adopted Revised Article 9 with a January 1, 2002 effective date.

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that “[a] filed record is effective only to the extent that it was filed by a person that may file it under Section 9-509.” The intent was to permit the filing office to provide a mechanism for quick and efficient filing, searching and retrieval of records by the public, specifically including by electronic means, without the filing office being involved in the accuracy of the information contained in such records. Article 9 contemplates that the final determiner of the accuracy of such information will be the courts – in the context of a proper case brought to them.

2. **Correction Statements:** The drafters of Article 9 recognized the potential problem of parties filing records wrongfully or containing errors. Section 9-518 allowed the filing by the debtor and other parties of a “correction statement” to place a party’s statement on the public record noting their disagreement without, however, affecting the effectiveness of the filed record. The drafters noted that Article 9 did not provide a complete solution to problems caused by misuse of the public records and invited “a summary *judicial procedure for correcting the public records and criminal penalties* for those who misuse the filing system”. (Emphasis added) *Comment 3, §9-518* While this invitation by the drafters can be cited to support the proposed Bill, you should note that the drafters stated that their recommendation for a judicial procedure “*are likely to be more effective and put less strain on the filing system than provisions authorizing or requiring action by filing and recording offices.*” *Comment 3, §9-518* Finally, please note that the use of correction statements in §9-518 is not limited to debtors. Secured parties may also avail themselves of this process, and applicable remedies should be available, if records constituting amendments (for example, deleting collateral, debtors or secured parties) or terminations are wrongfully filed – this problem is overlooked in the proposed Bill.

4. **The Debtor May File A Termination Statement:** In general, under revised Article 9 if no secured obligation is owed or will be owed by the debtor to the secured party, the secured party has an obligation under §9-513 to send to the debtor (in a commercial case) or to file (in a consumer case) a termination statement within the time limits set forth in §9-513. If the secured party fails to do so, Article 9 §9-509(d)(2) permits *the debtor* to file a termination statement, which has the effect of making the financing statement ineffective. Please note that, unlike former Article 9, whether a termination statement is filed by the secured party or by a debtor, the financing statement, with the termination shown as an amendment, will remain on file in the UCC records until one year after the financing statement lapses.

3. **Penalty Provisions and Private Remedies:** Article 9 provides civil remedies for making unauthorized filings in Section 9-625(b) and (e). Section 9-625(b) makes parties wrongfully filing such records liable for damages caused by the filing. In addition, a minimum statutory penalty of \$500.00 is provided under §9-625(e)(3) against any party that files a record that the person is not entitled to file. The Uniform Commercial Code, in section 1-103 (Conn. Gen. Stat. §42a-9-103), also incorporates supplemental principles of

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law and equity to permit parties to commence an action in equity to correct the UCC records or to obtain damages.

C. **Provisions from Other States:** Although an exhaustive search has not been performed, we have found two (2) other states, Pennsylvania and Texas, that have adopted provisions relating to wrongful filings;

1. **The Pennsylvania Statute:** Pennsylvania amended Article 9 §9-518 to add a subsection (d) which: (a) allows (but does not require) the Department of State to conduct an administrative hearing, whether or not a correction statement has been filed, to determine whether an initial financing statement was fraudulently filed; (b) provides that if the Department determines that a financing statement was wrongfully filed to place a *correction statement* in the UCC records, which correction statement creates a *rebuttable presumption* that the financing statement is ineffective; (c) provides an appeal mechanism to the Courts; and (d) states that it does not limit the remedies that a debtor has under the other provisions of Article 9. A copy of the Pennsylvania statute is attached to this testimony, for your information, marked "**Exhibit A**".

2. **The Texas Statute:** Texas adopted a new section (§9.5185) which does not provide for filing office involvement in determining effectiveness of records, but which does provide for private remedies of a minimum \$5,000.00 fee, court costs and reasonable attorneys fees upon any wrongful filing of a financing statement. The statute also provides for criminal penalties and equitable relief for the aggrieved party. A copy of the Texas statute is attached to this testimony, for your information, marked "**Exhibit B**".

**II. PROBLEMS AND RECOMMENDATIONS ON PROPOSED BILL**

A. **Problems From Mandatory Enforcement Action by Office of the Secretary of the State:** The proposed provision in new proposed subsection (d) of 9-518 [Section 2, subsection (d) of the Bill] requires the Secretary of the State to determine whether a record was wrongfully filed and to cancel any record which the secretary determines has been wrongfully filed. The Bill provides that upon such a finding the record will then become "void and of no effect", but subject to the appeal provisions in Section 3 of the Bill.

1. **The Proposed Revision Will Require Additional State Resources:** This Bill requires the Secretary of the State to conduct an investigation and to determine whether the contested record was wrongfully filed "without undue delay". This is a task that will require the Office of the Secretary of the State to provide personnel for a duty that is not presently conducted by that office. Given the short period of time that revised Article 9 has been in effect in the United States, in general, and in Connecticut, in particular, the Committee may wish to ask the Secretary to compile statistics and to determine whether

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there a significant problem exists and the required resources for such actions before it devotes the additional resources to this task.

**Recommendation:** Please consider either: (a) deleting the investigation function from this section of the Bill, until statistics are developed documenting a problem and leave private parties to their other remedies under Article 9 and common law; or (b) making the investigation by the Secretary of State *discretionary*, rather than mandatory, and expressly permitting private parties to exercise their remedies in the event that the Secretary of the State has not undertaken such an investigation.

2. **Rejection or Cancellation of a Financing Statement May Result In Loss of Priority During an Appeal:** The last sentence of the new proposed subsection (d) of 9-518 [Section 2, subsection (d) of the Bill] states that upon a finding by the Secretary of the State that a record was wrongfully filed the Secretary of the State shall “cancel the record and it shall be null void and of no effect.” Also the Secretary of State is permitted in Section 1 of the Bill to reject a financing statement if the Secretary finds that it was not “created” under Article 9 or intended for an “improper purpose”<sup>2</sup>. Both of these provisions are subject to the appeal rights in subsection (e) in Section 3 of the Bill, however during the appeal the effect of the Bill is to make the secured party automatically *unperfected*<sup>3</sup>.

**Recommendation:** Please consider adopting the provision in the Pennsylvania statute, allowing the Secretary of the State to file a correction statement noting its finding and adopting the rebuttable presumption that the financing statement is not effective. This would permit the filings to remain of record under the “open drawer” filing system during the time that an appeal is pending in the courts.<sup>4</sup> Another possibility would be to permit the financing statement to remain effective and indexed until the end of the appeal period or, if an appeal is filed, until the appeal is decided.

3. **Parties May Lose Their Article 9 and Common Law Remedies Pending Completion of Administrative Process:** The mandatory nature of the investigation procedure set forth in Section 2 of the proposed Bill, without more, leads to the

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<sup>2</sup> This provision is troubling, since the language is broader than the intent of the Bill – to restrain unauthorized or improper filings. The word “created” should be replaced by the word “authorized”.

<sup>3</sup> Since a cancelled record is “null, void and of no effect” under section 2 of the Bill and since a record rejected under amendment to §9-516(b) of the Bill is not entitled to the protection otherwise afforded a wrongfully rejected record under §9-516(d).

<sup>4</sup> This approach is consistent with the “notice filing” nature of the national UCC filing system and leaves to the courts the ultimate and final decision as to the effectiveness of UCC records, as contemplated by the drafters.

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conclusion that a Court will require debtors and other aggrieved parties to exhaust this administrative remedy before the Superior Court will entertain an action to remedy the same problem under Article 9 or under common law.<sup>5</sup>

**Recommendation:** Please consider adding a provision stating that the provision does not limit the remedies that a debtor or other party has under the other provisions of Article 9 or applicable law, as in the Pennsylvania statute.

**B. Limitation In Scope to Financing Statement:** This Bill deals only with wrongful or improper filing of a record constituting a financing statement. A secured party, or a debtor, may also be damaged by an amendment, a termination or similar record that is wrongfully filed.

**Recommendation:** Please consider whether this principle should also extend to amendments to financing statements filed by parties, including termination statements, and to correction statements<sup>6</sup> that are wrongfully filed.

**C. Correction Statement Nonuniformity:** Subsection (b)(3) of section 2 of the Bill, amending Article 9 §9-518(b)(3), requires a correction statement to include a "written certification under oath" as to the truth of the matters in the statement. This provision renders the national form of UCC correction statement unusable in Connecticut – prejudicing out of state parties and defeating the contemplated Article 9 goal of substantial national uniformity of forms. This provision will also make electronic submission of correction statements impossible, since the oath must be "written" – this defeats another primary goal of new Article 9, to ultimately permit UCC records to be filed and searched electronically.

**Recommendation:** Please consider deleting the written oath requirement. If an oath is required by the Committee, please instead consider a provision imposing civil or criminal liability upon a party that knowingly files a false correction statement without requiring a written oath – this would permit liability to attach for wrongfully filing a correction statement without harming national uniformity of forms and still ultimately allowing electronic filing of UCC documents.

**D. Criminal Provision – Effect on Pre-Filing in Commercial Cases:** The criminal provisions in Section 4 of the Bill impose criminal liability for filing any record "with knowledge that the record is not related to a valid security agreement" or with the intention that

<sup>5</sup> See, for example, *Connecticut Mobile Home Assn., Inc., v. Jensen's, Inc.*, 178 Conn. 586, 424 A.2d 285 (1979) and cases cited therein. "It is a settled principle of administrative law that, if an adequate administrative remedy exists, it must be exhausted before the Superior Court will obtain jurisdiction to act in the matter." *Id.* at 588

<sup>6</sup> Particularly if the Secretary of the State is required to conduct an investigation and to expend state resources upon a wrongful filing of a correction statement.

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it be filed for an improper purpose. Please note that it is a standard practice in commercial closings for secured parties to "pre-file" UCC financing statements before the closing of significant commercial transactions – to permit a UCC search to show their priority prior to conducting the closing. Normally, when the closing occurs the security documents ratify the earlier filings<sup>7</sup>. As noted above, if the closing does not occur, the secured party has an obligation to supply a termination statement or the debtor is authorized to file one. Under the proposed Bill this common commercial practice may constitute a criminal violation, since no security agreement was signed at the time that the record constituting a financing statement was filed – even if the transaction otherwise has nothing to do with Connecticut and out-of-state parties may not be aware of the provision. Although some parties obtain written consent from a debtor authorizing the secured party to file a financing statement before a closing, a criminal violation would still occur under this statute since a "valid security agreement" would not then exist.

**Recommendation:** Please consider adding after the phrase "with knowledge that the record is not related to a valid security agreement" the phrase ". . . , except when such record is filed in the good faith belief that a valid security agreement will be entered into by the debtor, . . .".

**III. CONCLUSION**

The goal of the proposed Bill, to protect innocent parties against the filing of unauthorized or wrongful financing statements is a laudable one.

However, Article 9 of the Uniform Commercial Code, which was substantially revised effective October 1, 2001, is an extremely complex statute governing a wide variety of commercial and consumer transactions. Therefore, amendments to Article 9 contemplated in the proposed Bill must be carefully reviewed in light of their potential unintended impact on commercial transactions, as well as to recognize the substantial changes in the effect of filing of records from prior law.

The proposed Bill, as presently drafted, will create a number of problems for commercial transactions in the State of Connecticut, as well as for out-of state transactions requiring filing of records within this state.<sup>8</sup>

<sup>7</sup> This practice was recognized by the drafters under Article 9, if ratification permitted under the "law with respect to ratification of past acts" governing the transaction. *Comment 3 to §9-509 and see Comment 3 to §9-502.*

<sup>8</sup> That there will be a significant impact upon the Office of the Secretary of State is also obvious. However, the Office of the Secretary of the State is the best position to advise the Committee on the affect of this Bill on its operations.

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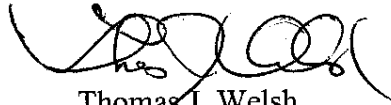
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I respectfully request that the Committee consider delaying any action on this Bill until we all obtain greater experience with problems resulting from the application of the new Article 9. However, in the event that the Committee determines that a statute should be adopted at this time, the foregoing materials provide an overview of the applicable law and comments as to changes to correct a number of problems.

Thank you.

Respectfully submitted,



Thomas J. Welsh

**EXHIBIT A**

**To**

**Testimony of Thomas J. Welsh**

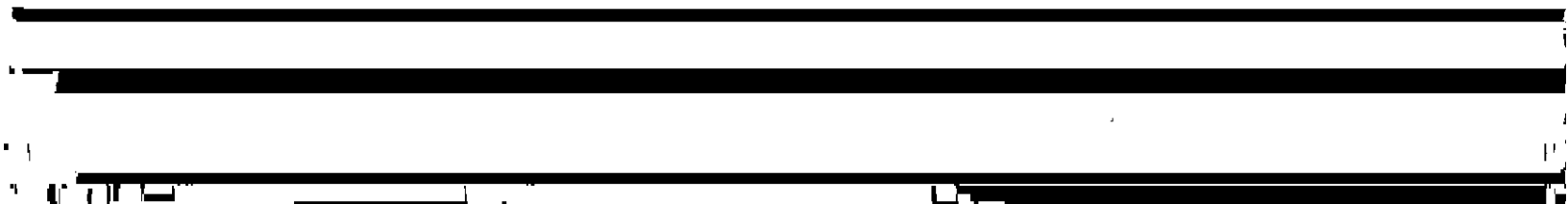
**Regarding SB 575**

**March 11, 2002**

**COPY OF PENNSYLVANIA STATUTE**

**BROWN & WELSH, P.C.**

MERIDEN EXECUTIVE PARK, 530 PRESTON AVENUE, POST OFFICE BOX 183, MERIDEN, CONNECTICUT 06450-0183



## SENATE BILL 330 P.N. 817

§ 9518. Claim concerning inaccurate or wrongfully filed record.

19 (a) Correction statement.--A person may file in the filing  
20 office a correction statement with respect to a record indexed  
21 there under the person's name if the person believes that the  
22 record is inaccurate or was wrongfully filed.

23 (b) Sufficiency of correction statement.--A correction  
24 statement must:

25 (1) identify the record to which it relates by the file  
26 number assigned to the initial financing statement to which  
27 the record relates;

28 (2) indicate that it is a correction statement; and

29 (3) provide the basis for the person's belief that the  
30 record is inaccurate and indicate the manner in which the

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1 person believes the record should be amended to cure any  
2 inaccuracy or provide the basis for the person's belief that  
3 the record was wrongfully filed.

4 (c) Record not affected by correction statement.--Except as  
5 provided in subsection (d), the filing of a correction statement  
6 does not affect the effectiveness of an initial financing  
7 statement or other filed record.

8 (d) Fraudulent financing statements.--

9 (1) The Department of State may conduct an  
10 administrative hearing to determine if an initial financing  
11 statement was fraudulently filed in accordance with the  
12 following:

13 (i) The hearing shall be conducted in accordance  
14 with 2 Pa.C.S. (relating to Administrative Law and  
15 Procedure). The department shall determine the initial  
16 financing statement to be fraudulently filed for purposes  
17 of this subsection if it determines that no rational  
18 basis exists under section 9509 (relating to persons  
19 entitled to file a record), entitling the person to file  
20 the initial financing statement and it appears that the  
21 person filed the initial financing statement with intent  
22 to annoy, harass or harm the debtor.

23 (ii) If the department determines that the initial  
24 financing statement was fraudulently filed and no timely  
25 appeal of the determination was filed, the department  
26 shall file a correction statement with respect to the  
27 initial financing statement indexed there. In addition to  
28 complying with the requirements of subsection (b), the  
29 correction statement filed by the department under this  
30 paragraph shall state all of the following:

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1 (A) the correction statement was filed by the  
2 department under this subsection;

3 (B) the department has determined that the  
4 initial financing statement was fraudulently filed  
5 and that the person had the right to appeal the  
6 decision to a court of competent jurisdiction;

7 (C) the initial financing statement found to be  
8 fraudulently filed may be ineffective; and

9 (D) the reasons why the department found the  
10 initial financing statement to have been fraudulently  
11 filed.

12 (iii) A correction statement filed by the department  
13 in accordance with paragraph (ii) creates a rebuttable

14 presumption that the initial financing statement found to  
15 be fraudulently filed is ineffective.

16 (iv) A person adversely affected by a determination  
17 of the department under paragraph (i) may appeal the  
18 determination in accordance with 2 Pa.C.S. § 702  
19 (relating to appeals).

20 (v) If the department determines that the initial  
21 financing statement was fraudulently filed and the  
22 determination is appealed to Commonwealth Court, the  
23 department shall file a correction statement with respect  
24 to the initial financing statement indexed there only  
25 upon affirmation by the court of its determination. In  
26 addition to complying with the requirements of subsection  
27 (b), the correction statement shall state all of the  
28 following:

29 (A) the correction statement was filed by the  
30 department under this subsection;

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1 (B) the department has determined that the  
2 initial financing statement was fraudulently filed  
3 and that the person had the right to appeal the  
4 decision to a court of competent jurisdiction;

5 (C) the initial financing statement found to be  
6 fraudulently is ineffective; and

7 (D) the reasons why the department found the  
8 initial financing statement to have been fraudulently  
9 filed.

10 (vi) If the department files a correction statement  
11 with respect to the initial financing statement indexed  
12 there under this subsection, it shall refer the matter  
13 for criminal prosecution to the Office of Attorney  
14 General pursuant to 18 Pa.C.S. § 4911 (relating to  
15 tampering with public records or information).

16 (2) Nothing in this subsection limits the rights or  
17 remedies the debtor may have with respect to an initial  
18 financing statement that has been fraudulently filed. Nothing  
19 in this subsection limits the effectiveness of a termination  
20 or correction statement filed by a debtor under sections  
21 9509(d)(2) and 9513 (relating to termination statement), or  
22 the rights of a debtor under section 9625 (relating to  
23 remedies for secured party's failure to comply with  
24 division).

**EXHIBIT B**

To

**Testimony of Thomas J. Welsh**

**Regarding SB 575**

**March 11, 2002**

**COPY OF TEXAS STATUTE**

**TEXAS LEGISLATURE ONLINE**

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## Bill History

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**Bill: SB 1058**

**Legislative Session: 76(R)**

**Council Document: 76R 05536**

**ENROLLED 06/18/1999 E Effective on ..... 07/01/2001**

Relating to the revision of the uniform law on secured transactions.

**Author:** Carona

**Sponsor:** Solomons

**Subjects:** I0050 Business & Commerce--General  
P0086 UNIFORM COMMERCIAL CODE-SECURED TRANSACTIONS

**Remarks:** This Act takes effect July 1, 2001 except that Section 2A.110, Business & Commerce Code, as added by Section 2.46 of this Act, and Subsection (f), Section 9.203, Business & Commerce Code, as added by Section 2.47 of this Act, take effect in 90 days (August 30, 1999).

**Senate Committee:** [Economic Development](#)

**Status:** Out

**Vote:** AYES= 5 NAYS= 0 PNV= 0 ABSENT= 2

**Bill Subcommittee:**

**House Committee:** [Business & Industry](#)

**Status:** Out

**Vote:** AYES= 7 NAYS= 0 PNV= 0 ABSENT= 2

**Bill Subcommittee:**

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**§ 9.518. Claim Concerning Inaccurate or Wrongfully Filed Record**

(a) A person may file in the filing office a correction statement with respect to a record indexed there under the person's name if the person believes that the record is inaccurate or was wrongfully filed.

(b) A correction statement must:

(1) identify the record to which it relates by the file number assigned to the initial financing statement to which the record relates;

(2) indicate that it is a correction statement; and

(3) provide the basis for the person's belief that the record is inaccurate and indicate the manner in which the person believes the record should be amended to cure any inaccuracy or provide the basis for the person's belief that the record was wrongfully filed.

(c) The filing of a correction statement does not affect the effectiveness of an initial financing statement or other filed record.

Added by Acts 1999, 76th Leg., ch. 414, § 1.01, eff. July 1, 2001.

**§ 9.5185. Fraudulent Filing**

(a) A person may not intentionally or knowingly present for filing or cause to be presented for filing a financing statement that the person knows:

(1) is forged;

(2) contains a material false statement; or

(3) is groundless.

(b) A person who violates Subsection (a) is liable to the owner of property covered by the financing statement for:

(1) the greater of \$5,000 or the owner's actual damages;

(2) court costs; and

(3) reasonable attorney's fees.

(c) A person who violates Subsection (a) also may be prosecuted under Section 37.101, Penal Code.

(d) An owner of property covered by a fraudulent financing statement described in Subsection (a) also may file suit in a court of suitable jurisdiction requesting specific relief, including, but not limited to, release of the fraudulent financing statement. A successful plaintiff is entitled to reasonable attorney's fees and costs of court assessed against the person who filed the fraudulent financing statement. If the person who filed the fraudulent financing statement cannot be located or is a fictitious person, the owner of the property may serve the known or unknown defendant through publication in a newspaper of general circulation in the county in which the suit is brought.

Business & Commerce Code - CHAPTER 9

Added by Acts 1999, 76th Leg., ch. 414, § 1.01, eff. July 1, 2001.